In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 488

UNITED STATES OF AMERICA, PETITIONER

v.

THE CITIZENS NATIONAL BANK OF EVANSVILLE, AS EXECUTOR

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY MEMORANDUM FOR THE UNITED STATES

1. Respondent states that "The basic principle underlying the marital deduction is that the spouse first to die shall be permitted to pass on to the surviving spouse, free of estate tax, up to one-half of his or her estate, *provided only that the terms of the transfer are such that this property will be taxable in the estate of the surviving spouse.*" (Br. Op. 3, emphasis added.) Building on this hypothesis, it then argues that the decedent's bequest to his widow qualifies for the marital deduction because the trust corpus will, by virtue of her general power of appointment over the trust assets, be included in her estate at her death. (See 1954 Code, § 2041, providing that a

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decedent's estate includes property over which she has a general power of appointment.)

Respondent has, however, misconceived the basic rationale of the marital deduction. If, as respondent contends, Congress had intended to grant a marital deduction to a decedent whenever assets in trust would be included in his surviving spouse's gross estate, then § 2056(b)(5)—the statutory provision here in question—would have provided for such a deduction in cases where the decedent left his widow only a general power of appointment over the trust corpus. However, that provision permits a marital deduction for trust assets only when the decedent has given his surviving spouse both a general power of appointment *and* "all the income" from the trust assets (or "all the income from a specific portion thereof") "for life," "payable annually or at more frequent intervals." § 2056(b)(5).

As explained in detail in our petition (Pet. 7–8), Congress intended the marital deduction to equalize the estate tax situation of decedents in common law and community property States.[1] Since, in a community property jurisdiction, the surviving spouse acquires absolute ownership over her one-half share of the community property, Congress declined to grant a marital deduction to a decedent in a common law state who left his surviving spouse an interest which was less than virtual ownership of trust assets. Thus

[1] Although inconsistent with its earlier statement that the "basic principle underlying the marital deduction" is to prevent taxation in both spouses' estates (Br. Op. 3), respondent concedes that the "purpose of the marital deduction was to extend to married taxpayers in common-law states the advantages of residents of community property jurisdictions" (Br. Op. 4).

the fact that the surviving spouse is given an interest (such as a general power of appointment) which is sufficient to require inclusion of the assets in her gross estate will not qualify the bequest for the marital deduction.[2]

2. Respondent's misunderstanding of the purpose of the marital deduction also leads it to urge an irrelevant ground for distinguishing the result in the instant case from the contrary result reached by the Third Circuit in *Northeastern Pennsylvania National Bank & Trust Co.* v. *United States* (Pet. App. B, pp. 23–46). Respondent urges that the marital deduction was properly denied in the *Northeastern Pennsylvania* case because invasion of corpus for the benefit of the widow in that case was probable, whereas in this case it is improbable. In fact, the actual or assumed existence of a power in the trustee to invade corpus in favor of the surviving spouse is completely immaterial in determining whether she has received a sufficient interest in the trust property to qualify for the marital deduction.

If the decedent had left the property here in question to his widow absolutely, it would undisputably have qualified for the marital deduction (even though she might prevent its inclusion in her estate by consuming it during her life). See, *e.g.*, 1954 Code, § 2056(a). If, however, he chooses to leave it in trust he must *at least* give her the right to all the income from the property (or all the income from a specific portion thereof) plus a general power of

[2] In such a case the Code ameliorates the burden of taxing the assets in both the husband's and the wife's estates by granting the second decedent a credit for the estate tax paid by the first decedent on the same assets. 1954 Code, § 2013.

appointment over it. 1954 Code, § 2056(b)(5). There is nothing in the Code to prevent him from giving her or a trustee greater power over the trust property exercisable solely in her favor. For example, the trust would still qualify for the marital deduction even if the decedent had also given his widow the power to withdraw the corpus at her discretion, or if he had given the trustee the power to pay the corpus to her at its discretion, or if he had directed the trustee to terminate the trust at the end of five years and pay all of the corpus to his widow.

Therefore, the bequest in the *Northeastern Pennsylvania* case could not have been disallowed because the trustee might have invaded corpus to maintain the stated payments to the widow. In fact, the Third Circuit acknowledged that the two cases were indistinguishable with respect to the issue presented and denied a marital deduction because it disagreed with the Seventh Circuit's holding in the instant case (Pet. 38). Consequently, review by this Court is necessary in order to resolve the direct conflict between the circuits on this important question in the administration of the Internal Revenue laws.

Respectfully submitted.

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